



INFORMATION REPORT

TO:	Chair and Members Audit, Finance and Administration Committee
COMMITTEE DATE:	September 14, 2015
SUBJECT/REPORT NO:	2014 Standard & Poor's Credit Rating (FCS15057) (City Wide)
WARD(S) AFFECTED:	City Wide
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SIGNATURE:	

Council Direction:

N/A.

Information:

Standard & Poor's Rating Service (S&P) has reviewed the City of Hamilton's (Hamilton) credit rating and affirmed the rating at AA with a "stable" outlook.

S&P's credit rating documents, attached to Report FCS15057, include:

- Appendix "A" to Report FCS15057 S&P's "Supplementary Analysis" printed and released on June 26, 2015.
- Appendix "B" to Report FCS15057 S&P's "Press Release" dated June 24, 2015.

Rationale:

On May 27, 2015, City staff met with S&P analysts and provided requested information which included operational reports, budget information, financial information reports, financial statements and an economic development review. The analysts reviewed the information supplied and performed an analysis of the City's current financial position and its projected financial position going forward. This analysis was presented to their credit committee and the City's credit rating was affirmed as AA (Stable) in the subsequent "Press Release" and "Supplementary Analysis" released on June 24 and June 26, 2015 respectively.

In the "Press Release" and the "Supplementary Analysis", the City's rating score snapshot was summarized as follows:

KEY RATING FACTORS	ASSESSMENT
1) Institutional framework	Very Predictable and Well Balanced
2) Economy	Very Strong
3) Financial Management	Strong
4) Budgetary Flexibility	Average
5) Budgetary Performance	Strong
6) Liquidity	Exceptional
7) Debt Burden	Low
8) Contingent Liabilities	Very Low

Explanations:

- 1) Canadian municipalities benefit in general from a very predictable and well-balanced local and regional government framework that has demonstrated a high degree of stability and are legislated to pass balanced operating budgets.
- 2) Hamilton's economy is viewed by S&P as very strong and as moving to a more diversified economy with lessened contribution by its traditional manufacturing base. Population growth has been slower than that of Ontario, but unemployment remains lower than the Provincial level and the City has fair prospects for growth and further diversification.
- 3) Financial Management is strong. Disclosure and transparency are very good. Financial statements are audited and unqualified. Annual operating and capital budgets integrate with the City's strategic direction. Robust and well defined financial policies guide debt and investment management.
- 4) Budgetary Flexibility is average due to provincially mandated service levels, labour contracts, inflation, and political pressures. However, they are constrained by economic and political pressures. Hamilton has a lower average household income and a large infrastructure deficit which both influence flexibility.
- 5) Budgetary Performance is expected to be average with strong operating balances of about 11% of operating revenues, and after-capital deficits not exceeding 5% of total revenues through 2017.
- 6) Hamilton's exceptional liquidity has a positive impact on its credit profile. Sufficient adjusted free cash and liquid assets forecast to December 31, 2015 are expected to cover approximately 9.0x debt service costs for 2016. While liquidity levels may be reduced in the medium term, it is expected that coverage will remain exceptional.

- 7) Hamilton's debt burden is considered low at December 31, 2014. The debt level is expected to increase moderately possibly reaching 33% of operating revenue by the end of 2017, but interest costs will remain at less than 5% of operating revenue throughout 2016 and 2017.
- 8) Contingent liabilities are very low. The City owns Hamilton Utilities Corporation (HUC) whose primary business is electricity distribution. However, HUC is viewed as self-supporting and not in need of material support. Hamilton's contingent liabilities stem largely from standard employee benefits and landfill post-closure liabilities and are considered very low. They represent about 11% of consolidated operating revenues and 9% of net dedicated reserves in 2014, and do not have a significant impact on the City's credit profile.

Hamilton has three defined benefit pension plans and other retirement benefits with a total liability at the end of 2014 of \$C177 million, which represents 12.7% of operating revenue. The annual service cost for these plans is not significant and is comfortably incorporated into Hamilton's operating budget.

In summary, S&P concluded that Hamilton scores very well in 7 of 8 rating factors with above average rankings up to and including an exceptional rating for liquidity. Budgetary flexibility and performance are rated as average to strong due for the most part to constraints of household income and a large infrastructure deficit.

Financial Ratios:

S&P has concentrated on 5 ratios in evaluating the City's and other municipalities score specifically for credit ranges such as AA-, AA (Stable), AA+. Four of these ratios appear in the Table below and in Table 2 of Appendix "A" to Report FCS15057. The 5th ratio appearing in the Table below is discussed under heading: "We Expect That Liquidity Balances Will Decrease In the Medium Term But Remain Exceptional" in Appendix "A" to Report FCS15057. The 5 ratios are shown in the Table below with the City's 2014, 2013 and 2012 ratios and the 2013 average for the full range of AA municipalities rated by S&P.

Year	Operating Balance as a % Adjusted Operating Revenues	Balance After Capital Accounts as a % of Total Revenues	Capital Expenditures as a % of Total Expenditures	Tax-Supported Debt as a % of Consolidated Operating Revenues	Free Cash and Liquid Assets Plus Committed Facilities as a % of Next 12 Months Debt Service
Hamilton 2014	11.7%	(1.9%)	22.8%	31.4%	1150%
Hamilton 2013	11.8%	(1.7%)	18.7%	28.4%	1125%
Hamilton 2012	11.9%	4.2%	21.6%	31.9%	1252%
Average of Municipal Comparators 2013 (AA)	12.7%	(1.8%)	21.0%	54.6%	883%

In 2014, the operating return declined marginally to 11.7% from 11.8% in 2013, which indicated negligible change in net operating revenue. The balance after capital declined to a negative percentage of -1.9% versus -1.7% in 2013. The capital expenditures increased to 22.8% versus 18.7% in 2013 reflecting an increase in capital expenditures. The tax supported debt increased to 31.4% from 28.4% in 2013. The free cash and liquid assets increased marginally to 11.50x from 11.25x in 2013. S&P has developed this ratio to assess the capability of a municipality to meet the next 12 months debt service. S&P rates 35 Canadian municipalities and 24 (69%) are considered "exceptional" with this ratio being greater than 1.0x.

Outlook:

The stable outlook reflects an expectation that over the 2 year horizon, Hamilton will maintain exceptional liquidity balances and after capital deficits will not exceed 10% of total revenue, and tax supported debt will remain less than 60% of consolidated operating revenue. The outlook could be revised to "positive" or the rating raised if the City experiences strong revenue growth, effective cost containment, substantial deferrals of capital spending and associated debt issuance resulting in significantly stronger operating balances, after capital surpluses, and tax supported debt not materially not exceeding 30% of operating revenue. Although unlikely in the next 2 years, the outlook could be revised to "negative" or the rating lowered if the City does not meet these expectations and long-term trends indicated continuing erosion of its credit profile.

Hamilton's Credit Rating History

Rating Agency	Rating (Note 1)
Standard & Poor's (<u>formerly CBRS</u>)	AA: 2008 - 2014 AA/Positive: 2005 - 2007 AA: 1999 to 2005 AA+: 1994 to 1999 AAA: 1989 to 1994
Moody's	Aa3: 1995 to 2001 Aa2: 1988 to 1995
Dominion Bond Rating Service	AA: 2004 to 2009 AA+: 1994 to 2004

Note 1: Table provides ratings for City of Hamilton from 2001 to 2014 and ratings for Regional Municipality of Hamilton-Wentworth from 1988 to 2000.

Peer Comparison Using Standard & Poor's Rating

Municipality (Single Tier City or Regional Municipality)	Rating (Stable outlook if not stated otherwise)
Durham	AAA
Halton	AAA
London	AAA
Peel	AAA
Waterloo	AAA
Brantford	AA+
Guelph	AA+
Ottawa	AA+
Regina (Sask)	AA+
York	AA+
Barrie	AA
Hamilton	AA
Kingston	AA
Niagara	AA
Toronto	AA
Windsor	AA